

BEFORE THE
ATTORNEY GENERAL OF CALIFORNIA
STATE OF CALIFORNIA

In the Matter of the First Amended Order to
Cease and Desist, Revocation of California
Charity Registration and Assessment of
Penalties Against:

Case No. 2018-CT086331

OAH No. 2018050194

FOOD FOR THE POOR, INC.,

Respondent.

DECISION

The attached Proposed Decision of the Administrative Law Judge is hereby adopted by the Department of Justice as its Decision in the above-entitled matter.

This Decision shall become effective on September 6, 2019.

IT IS SO ORDERED this 6th day of September, 2019.

By: _____



Jonathan L. Wolff
Chief Assistant Attorney General
Division of Civil Law



OFFICE OF ADMINISTRATIVE HEARINGS

State of California

GENERAL JURISDICTION DIVISION

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Department of General Services

Governor Gavin Newsom

May 24, 2019

Department of Justice - Charitable Trusts Section
Registry of Charitable Trusts
1300 I Street
Sacramento, CA 95814
Attn: Executive Director

RECEIVED
Attorney General's Office

MAY 29 2019

Registry of
Charitable Trusts

Subject: Food for the Poor, Inc.
OAH No. 2018050194
Agency No. 2018-CT086331

Enclosed are the following:

- ☒ The original Proposed Decision
- ☒ An agency order of adoption. If the Proposed Decision is adopted, please return a copy of the signed adoption order to the Office of Administrative Hearings.
- ☐ The original Decision
- ☒ Exhibits numbered: *To Follow*
Please make sure you have received all listed exhibits. If exhibits are missing, please contact OAH immediately.
- ☐ Email copy of the Proposed Decision to:
- ☐ The above referenced case was resolved prior to conclusion of the hearing. We are returning the enclosed original exhibits 1 - x to you.

ref

Encl.

Transmittal Form
OAH 60 (Rev. 04/09)

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The attached Proposed Decision of the Administrative Law Judge is hereby adopted
by the Department of Justice - Charitable Trusts Section as its Decision in the above-entitled
matter.

This Decision shall become effective on _____.

IT IS SO ORDERED this _____ day of _____.

By: _____

BEFORE THE
ATTORNEY GENERAL OF CALIFORNIA
STATE OF CALIFORNIA

In the Matter of the First Amended Order to
Cease and Desist, Revocation of California
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PROPOSED DECISION

Administrative Law Judge Thomas Heller, State of California, Office of Administrative Hearings, heard this matter in Los Angeles, California from November 27 through December 12, 2018. It was consolidated for hearing with cases against two other charities: *In re Catholic Medical Mission Board, Inc.* (Case No. 2018-13-5602319, OAH No. 2018050397), and *In re MAP International* (Case No. 2018-CT103136, OAH No. 2018050401). A separate proposed decision is being issued in each case. (Cal. Code Regs., tit. 1, § 1016, subd. (d).)

Sonja K. Berndt, and Jami L. Cantore, Deputy Attorneys General, represented complainant David Eller, Registrar of the Registry of Charitable Trusts. Sandra Barrientos, Deputy Attorney General, also represented complainant on December 7, 2018, and during post-hearing oral argument.

Tracy L. Boak, Esq., and Adam D. Miller, Esq., Perlman and Perlman LLP, represented respondent Food for the Poor, Inc. (FFP).

At the end of the hearing, the administrative law judge held the record open for the parties to submit closing briefs. Complainant filed a brief on January 11, 2019; FFP, Catholic Medical Mission Board, Inc. (CMMB), and MAP International, Inc. (MAP) filed briefs on February 11, 2019; and complainant filed a reply brief on February 25, 2019. The briefs were marked for identification as exhibits 1058 through 1062. CMMB also lodged the transcripts of the hearing.

On February 28, 2019, CMMB lodged an exhibit used at the hearing to which complainant objected. On March 8, 2019, the administrative law judge ordered the exhibit

marked but not admitted and deemed the matters submitted. On April 3, 2019, the record was reopened for oral argument, which was held on April 24, 2019, after which the matters were deemed resubmitted.

SUMMARY

FFP is a charity that facilitates shipments of donated pharmaceuticals to indigent populations in developing countries, among other charitable programs. To help fund its operations, FFP solicits monetary donations from persons in California and elsewhere. Complainant alleges FFP inflated the value of the pharmaceuticals in its financial reporting to make it appear to the public that FFP was a larger and more efficient charity than it actually was. FFP used United States market prices to value the pharmaceuticals, and complainant alleges that doing so was inconsistent with generally accepted accounting principles (GAAP), which charities that solicit donations in California must follow. Complainant also alleges FFP's solicitations for monetary donations were deceptive about how efficient FFP was in using monetary donations for charitable purposes. FFP asserts it properly valued the pharmaceuticals and that its solicitations were not deceptive.

Complainant did not prove that FFP's use of United States market prices to value the pharmaceuticals departed from GAAP. The evidence that the valuations complied with GAAP had more convincing force than the evidence opposed to it. But complainant did prove that FFP's solicitations for monetary donations were deceptive in implying that FFP used 95 percent of all money donated for charitable programs, which it did not. FFP really used less than 70 percent of monetary donations for charitable programs, and used the rest for administration and fundraising. A cease and desist order and penalties are warranted to address the deceptive solicitations. These remedies are sufficient to protect the public from further violations, so complainant's additional request for revocation of FFP's California charity registration will be denied.

FACTUAL FINDINGS

Statement of Facts and Procedural History

1. FFP is a nonprofit charitable corporation based in Florida. Its stated charitable purpose is to improve the health, economic, and social conditions of the poor throughout the world. FFP solicits monetary donations in California in support of its charitable efforts, requiring it to be registered with the California Attorney General's Registry of Charitable Trusts under the Supervision of Trustees and Fundraisers for Charitable Purposes Act (Gov. Code, § 12580 et seq.).¹ Furthermore, as a charitable organization soliciting in California, FFP is subject to the annual reporting requirement and other provisions of the Supervision of Trustees and Fundraisers for Charitable Purposes Act, and must maintain its financial records

¹ Undesignated statutory references are to the Government Code.

in accordance with GAAP (Bus. & Prof. Code, § 17510.5, subd. (a)). GAAP refers to the set of accounting principles established by the Financial Accounting Standards Board (FASB) in order to ensure that financial reporting is transparent and consistent from one organization to another.

2. FFP facilitates shipments of donated goods, such as donated pharmaceuticals, food, and clothing, to developing countries, primarily in the Caribbean, Latin America, and South America. With respect to donated pharmaceuticals, other United States charities receive donations from United States pharmaceutical companies and then partner with FFP to deliver them to developing countries. During the time period relevant to this case, a typical donation transaction occurred as follows:

a. A pharmaceutical company offered another charity (e.g., CMMB or MAP) a donation of a large quantity of pharmaceuticals, often close to the expiration date of the pharmaceuticals;

b. The other charity advised FFP of the available pharmaceuticals, quantities, and expiration dates;

c. FFP advised one of its foreign-organization beneficiaries of the available pharmaceuticals, and the foreign organization accepted or rejected the offer;

d. FFP notified the other charity when the foreign organization accepted the offer;

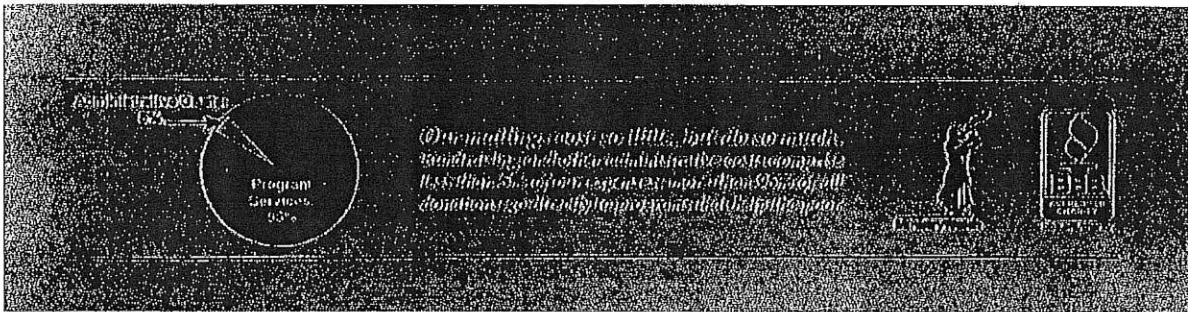
e. The drugs were shipped from the other charity's warehouse to the selected foreign-organization recipient.

3. For 2012 through 2015, FFP reported annual revenue of \$900 million to \$1.16 billion, with donations of pharmaceuticals and medical supplies comprising 54 to 71 percent of that revenue. For the same years, FFP reported annual program expenses of \$859.47 million to \$1.12 billion, with pharmaceuticals and medical supplies distributed in other countries comprising 56 to 73 percent of those expenses.

4. The United States pharmaceutical companies have typically restricted the donated pharmaceuticals to distribution and use outside the United States. During the years described above, FFP nonetheless used United States market prices to value the pharmaceutical donations it received (as revenue), and to value the pharmaceuticals it sent to other countries in partnership with other charities (as program expenses). FFP then reported those revenue and program expenses on its annual Internal Revenue Service Form 990, which it filed with the Attorney General's Registry of Charitable Trusts along with an annual Registration Renewal Fee Report (Form RRF-1). FFP's audited annual financial statements also included the same revenue and expense figures.

5. FFP also used those revenue and expense figures in formulating its charitable solicitations for monetary donations. From at least 2012 through 2015, those solicitations typically stated that FFP was more than 95 percent efficient in using gifts for programs. These statements were based on FFP's combined cash (i.e., monetary) and gift-in-kind (GIK) revenues and expenses, with the GIK amounts largely attributable to pharmaceutical donations.

6. The solicitations typically stated, "Our mailings costs so little, but do so much. Fundraising and other administrative costs comprise less than 5% of our expenses; more than 95% of all donations go directly to programs that help the poor." (See Exhibits 144-149, 151-152, 153 [Spanish version].) Another version stated, "Food for the Poor is a good steward of your gifts. More than 95% of all donations go directly to programs that help the poor." (Exhibits 149-150.) The solicitations also included a pie chart depicting 95 percent of donations as funding program services and less than five percent of donations as funding administrative costs, as follows:



(Exhibit 148, p. FL0001315; see also Exhibits 144-153.)

7. From 2013 through 2015, FFP sent 948,958 solicitations containing such a statement (the "95% Statement") to persons in California. (Exhibit 143.) Between 2012 and 2015, FFP collected more than \$38 million through more than 700,000 donations from Californians in response to its mail solicitations. (Exhibit 142.)

8. In February 2016, Tania Ibanez, the Senior Assistant Attorney General for the Attorney General's Charitable Trusts Section, received a Spanish-language solicitation from FFP containing the 95% Statement described above. The Charitable Trusts Section began investigating FFP, which ultimately led to investigations of MAP and CMMB as well. On March 7, 2018, complainant filed an Order to Cease and Desist against FFP, which complainant amended a few days later. The first amended order alleged FFP improperly used United States market prices to value donated pharmaceuticals even though the donations were restricted to distribution and use outside the United States. According to complainant, the valuations did not comply with GAAP, resulting in overstatements of FFP's size and efficiency in using donations for charitable programs (as opposed to for administration and fundraising). Complainant also alleged FFP's solicitations to California donors were deceptive in suggesting that FFP used 95 percent of monetary donations for

charitable programs, when it actually used a smaller percentage of monetary donations for such programs. Complainant filed similar cease and desist orders against CMMB and MAP, which also valued donated pharmaceuticals using United States market prices and made similar percentage efficiency statements in their solicitations.

9. Regarding the solicitations, the first amended order directed FFP to cease and desist from "including the '95% Statement' in its solicitations to California donors (or other percentages of combined cash and non-cash donations used for programs)." (Exhibit 1.4, First Amended Order to Cease and Desist against FFP at p. 21.) The first amended order also assessed \$88,000 in penalties against FFP for making materially false statements in its IRS Forms 990 and Forms RRF-1 and for failing to maintain its financial records in accordance with GAAP, and another \$1,000,000 in penalties for "making representations in its solicitations to California donors that were false and deceptive, and created a likelihood of confusion or misunderstanding." (*Id.* at pp. 11-21.) Finally, the first amended order requested revocation of FFP's charity registration with the Attorney General's Registry of Charitable Trusts. (*Id.* at pp. 22-23.)

10. FFP timely appealed the first amended order, and the case was consolidated for hearing with the similar orders against CMMB and MAP. The administrative law judge ordered the issue of whether the three charities complied with GAAP to be heard first through the testimony of expert witnesses. Thereafter, the administrative law judge heard evidence on the alleged solicitation violations.

GAAP Compliance

COMPLAINANT'S EXPERTS

11. Complainant called two experts in the first phase of the hearing: (1) Joel H. Hay, Ph.D., a pharmaceutical economist; and (2) Craig Stevens, a certified public accountant. Dr. Hay testified about the differences between the United States and international pharmaceutical markets, and opined that the principal markets for the donated pharmaceuticals were international markets, not the United States market, because the pharmaceutical companies restricted the donations to distribution and use outside the United States. According to Dr. Hay, the proper source for valuing the pharmaceuticals was an international pricing guide published by the nonprofit organization Management Sciences for Health. The guide contains a variety of prices from pharmaceutical suppliers, international development organizations and charities, and government agencies, and generally reflects much lower prices than United States market prices, at least for branded drugs. Using the guide and a calculation formula he developed, Dr. Hay computed much lower prices for the donated pharmaceuticals than the charities reported, and concluded that the charities' use of United States market prices overstated the fair market value of the pharmaceuticals. Dr. Hay is not an accountant or expert on GAAP, but expressed these opinions from the standpoint of an economist.

12. Mr. Stevens testified as an accounting expert in nonprofit audits and GAAP. He retired in 2017 from the accounting firm Aronson, LLC, after leading the firm's nonprofit group and performing over 1,000 audits of nonprofit organizations. Mr. Stevens opined that the charities' use of United States market prices to value the donated pharmaceuticals did not comply with GAAP, because the donations were restricted to distribution and use outside the United States. Therefore, the charities did not maintain their financial records in accordance with GAAP.

13. Under GAAP, an entity must report the "fair value" of an asset or liability, which is "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date." (FASB Accounting Standards Codification (ASC) 820-10-35-2.) GAAP also requires charities to use the "principal market" in valuing an asset or liability, or the "most advantageous market" in the absence of a principal market. (FASB ASC 820-10-35-5.) Charities must have access to the principal or most advantageous market in valuing the asset or liability. (FASB ASC 820-10-35-6A.) "In the absence of evidence to the contrary, the market in which the reporting entity normally would enter into a transaction to sell the asset or to transfer the liability is presumed to be the principal market or, in the absence of a principal market, the most advantageous market." (FASB ASC 820-10-35-5A.)

14. Mr. Stevens opined that the United States market was not the principal market for the donated pharmaceuticals because of the donor-imposed restrictions on the distribution and use of the pharmaceuticals. According to Mr. Stevens, the charities lacked access to the United States market because of these restrictions, and the specific countries where the donations were distributed were the principal markets for purposes of valuing the pharmaceuticals under GAAP.

15. On cross-examination, Mr. Stevens acknowledged that the fair value measurement for a donation of pharmaceuticals depends on hypothesizing a sale between market participants, since a donation is not a sale. He also acknowledged that his position was inconsistent with a 2018 audit risk alert to not-for-profit entities from the American Institute of Certified Public Accountants (AICPA), the world's largest member association representing the accounting profession. Although non-binding on GAAP compliance, the risk alert indicated that a donor-imposed restriction to use a pharmaceutical outside the United States does not affect the valuation of the pharmaceutical under GAAP:

GIK use is often subject to donor restrictions and sometimes legal restrictions. An NFP [i.e., not-for-profit] needs to be thorough in understanding which restrictions are characteristics of the donated assets (and, thus, are restrictions that affect valuation) and which are donor-imposed use restrictions (which are entity restrictions that affect classification of net assets but don't affect measurements of fair value). For example, when pharmaceuticals are from sources in foreign countries (and, thus, unable to be sold in the United

States because the pharmaceuticals do not meet US. Food and Drug Administration standards), it is a best practice to assume a rebuttable presumption that international market prices should be used to determine fair value. The inability of the pharmaceutical to be sold in the U.S. marketplace is an asset characteristic to be considered in valuing the GIK. However, a donor-imposed restriction to use the pharmaceutical in Africa is a donor-imposed use restriction, which affects the classification of the contribution revenue but not the valuation of the GIK.

(Exhibit 703, pp. 004-005.)

16. Mr. Stevens also admitted his position conflicted with some material in the AICPA's Audit and Accounting Guide, and with the opinions of the auditing firms for FFP, CMMB, and MAP. He also acknowledged that GAAP can potentially have two correct answers in circumstances such as the present case. After discussing these facts, counsel for CMMB asked Mr. Stevens if he remained confident in his opinion, and Mr. Stevens testified he had reservations about his opinion and that his percentage of confidence in it was "dropping."

Q Okay. So sir, based on everything we've talked about, your testimony over the last two days, do you have any reservations about your position, the one that is inconsistent with GAAP -- with the AICPA?

A Do I have any reservations? Yes, sure.

Q One of the reasons you have reservations we talked about earlier; right? GAAP is one of those things that is subjective determinations; right? And it is even possible in circumstances like this to have two correct answers; right?

A Potentially.

Q Okay. After all you've seen, sir, what is your percentage confidence that you are right and everybody on this side is wrong?

A It's dropping.

(Transcript, Vol. V, pp. 929-930.) Complainant did not examine Mr. Stevens on redirect after this testimony.

RESPONDENTS' EXPERTS

17. FFP, CMMB, and MAP called three experts: (1) Linda MacDonald, an accounting expert for MAP; (2) Eltjo Schoonveld, a pharmaceutical industry pricing consultant; and (3) Bruce Richman, an accounting expert for all three charities. Ms. MacDonald is a certified public accountant and certified fraud examiner who worked for FASB for about 12 years, and was the lead at FASB for the fair value project that issued the guidance in FASB Statement 157, which is now codified in FASB ASC 820, the GAAP standard for measuring fair value.

18. Ms. MacDonald testified that Mr. Stevens erred in his interpretation of GAAP, and did not apply the definitions of GAAP as they were intended to be applied. She further opined that the donor-imposed restrictions on the use of the pharmaceuticals had no bearing on the determination of the principal market for a fair value measurement under GAAP, and were not the types of restrictions that would otherwise affect the value using the pricing in the principal market for a fair value measurement.

19. In Ms. MacDonald's opinion, the fatal flaw in Mr. Stevens's approach was his initial assumption that there is a transaction to distribute or donate the particular product outside the United States. The correct approach is not to assume the actual use of the product, but rather to value it in the market without regard to whether, how, and where the product will be actually used. According to Ms. MacDonald, Mr. Stevens did the opposite by looking first at how the donations would be used, which resulted in an entity-based measurement, not a market-based measurement as contemplated under GAAP. GAAP does not use entity-based measurements, and required MAP not to consider the actual use of the product the fair value measurement. The nature of the donation transactions from United States pharmaceutical companies to a United States charity indicated that the principal market was the United States market. Furthermore, the requirement that a reporting entity must have access to the principal market does not change this analysis, because the donor-imposed restrictions on distribution and use of the pharmaceuticals were entity-based restrictions that should not be considered under GAAP.

20. Mr. Schoonveld testified that it was inappropriate for Dr. Hay to use the Management Sciences for Health pricing guide in valuing the donated pharmaceuticals. The guide does not include information from pharmaceutical manufacturers, and the information in it is sparse. According to Mr. Schoonveld, the more appropriate and complete source for pricing is the Wholesale Acquisition Cost (WAC), a United States market-based measurement of pharmaceutical costs. The prices in the Management Sciences for Health guide were much lower than in the private international markets for pharmaceuticals.

21. Bruce Richman, a certified public accountant, is the national director of the business investment global valuation advisory practice of Mazars USA, an accounting and consulting firm. Like Ms. MacDonald, Mr. Richman opined that the United States market was the principal market for purposes of a GAAP valuation, and testified that the charities' valuations of the donations were correct. Mr. Richman gives significant weight to AICPA

interpretations of GAAP, and has never departed from AICPA guidance. He agreed with Ms. MacDonald's opinions with respect to all three charities.

DISCUSSION OF GAAP COMPLIANCE

22. The charities' evidence of GAAP compliance had more convincing force than the evidence opposed to it. In particular, the testimony of Ms. MacDonald and Mr. Richman was more persuasive on the GAAP valuation issues than Mr. Stevens's testimony, and supported the charities valuing the pharmaceutical donations according to United States market prices. Ms. MacDonald and Mr. Richman rebutted Mr. Stevens's testimony, and Mr. Stevens questioned his own interpretation of GAAP by the end of his testimony, stating that his confidence in his opinion was "dropping." Furthermore, the AICPA audit risk alert from 2018 is directly on point and supports the charities' position. Although not authoritative on GAAP compliance, the AICPA risk alert is consistent with the testimony of Ms. MacDonald and Mr. Stevens and supported the charities valuing the donated pharmaceuticals as they did, despite the restrictions on the distribution and use of those donations to locations outside the United States. The charities' independently-audited financial statements also supported those valuations and evidenced multiple other accountants certifying the valuations as complying with GAAP. Therefore, the weight of the evidence on GAAP compliance was that the charities complied with GAAP in their valuations of the donated pharmaceuticals.

Solicitations

COMPLAINANT'S WITNESSES

23. Complainant called two witnesses regarding the charities' solicitations: (1) Ms. Ibanez; and (2) Stevens Bauman, a Supervising Investigative Auditor in the Attorney General's Charitable Trusts Section. Ms. Ibanez testified that the Charitable Trusts Section assists the Attorney General in his oversight of charities and professional fundraisers, and is the section that investigated and prosecuted this case.

24. Ms. Ibanez testified she was concerned about the solicitation she received from FFP in 2016 because she knew mail solicitations were extremely expensive, which made her doubt the accuracy of the statement in the solicitation that less than five percent of FFP's expenses were administrative expenses. Her concern led to the investigation of FFP, which in turn led to the investigations of CMMB and MAP. Ms. Ibanez noted that only monetary donations can pay for administrative expenses and fundraising, and opined that a typical donor would not realize what percentage of donations are monetary versus GIK. In Ms. Ibanez's opinion, even if the charities followed GAAP, their percentage efficiency statements were misleading because the vast majority of revenue and expenses used in the percentage efficiency calculations were GIK that could not be used to pay for administrative and fundraising expenses.

25. Mr. Bauman has been an auditor in the Charitable Trusts Section for 30 years. He conducted an analysis of the charities' respective Forms 990 for the years at issue and

found that 25 percent to 40 percent of the charities' monetary donations were used to pay for administrative, management, and general expenses, rather than for program services. For FFP in particular, he found less than 70 percent (not 95 percent) of FFP's monetary donations went to program services. (Transcript, Vol. VIII, pp. 1493-1495.) He reached this result by comparing FFP's reported revenues to its program and other expenses.

FFP'S EVIDENCE

26. FFP called Jeffrey Alexander, its controller, to testify about the solicitations and FFP's operations and finances. Mr. Alexander has been FFP's controller for 18 years, and worked for the charity for 25 years. He testified that FFP is a faith-based organization that provides material needs to enhance the lives of the poor. At least 85 percent or 90 percent of FFP's revenue stream comes from GIK, although cash pays for all salaries, fundraising and administrative costs. FFP's cash donors are primarily individuals, although foundations, private corporations, and estates also contribute.

27. Mr. Alexander testified that FFP's percentage efficiency statements are correct as a statement of "total program efficiency," referring to both GIK and monetary donations. The percentage efficiency statements come from directly from FFP's financial statements, which are audited by an independent accounting firm. FFP uses those efficiency statements in its solicitations, its annual report, and on its website, and provides financial data to charity watchdog organizations, such as the Better Business Bureau Wise Giving Alliance, which independently report that 95 percent of FFP's expenses are for charitable programs.

28. Under questioning from complainant's counsel, Mr. Alexander testified that since the Attorney General's audit, about two thirds of every monetary donation to FFP actually goes to programs, as opposed to administration and fundraising. He did not know the percentage prior to that.

DISCUSSION OF SOLICITATION EVIDENCE

29. Mr. Alexander's testimony that the percentage efficiency statements in the solicitations were accurate with respect to FFP's donations as a whole is not determinative on whether the solicitations were deceptive. A statement may be accurate on some level but still be deceptive, e.g., by failing to disclose other relevant information. At the same time, Ms. Ibanez's opinion that the charities' solicitations were deceptive does not prove they were. The Charitable Trusts Section is prosecuting this case, and Ms. Ibanez's personal opinion as the leader of that section is not proof of a violation. Resolution of complainant's allegations concerning the solicitations requires determining whether a deceptive character appears on applying the words of the solicitations to the facts without regard to that opinion.

30. FFP's solicitations stated that "more than 95% of all donations go directly to programs that help the poor," and included a pie chart depicting 95 percent of donations as funding program services and 5 percent as funding administrative costs. These statements implied that more 95 percent of the gifts being solicited – i.e., monetary gifts – would be

used for charitable programs, and that less than five percent would be used for administration or fundraising. But FFP only used the stated percentages of gifts for charitable programs when considering both monetary and in-kind gifts. When considering just monetary gifts, FFP used under 70 percent of gifts for charitable programs. None of the solicitations stated that lower percentage, and thus none of them accurately described FFP's efficiency in using the monetary gifts being solicited for charitable programs.

31. Most of the solicitations prefaced the 95% Statement with the sentence "Our mailings cost so little but do so much," linking the percentage to the monetary gifts requested in FFP's mailings. Two solicitations prefaced the 95% Statement with "Food for the Poor is a good steward of *your gifts*" (emphasis added), creating an even more direct link. This phrasing implied that the stated percentage applied to the monetary gifts being solicited, which it did not. Thus, the solicitations were couched in a manner that was likely to deceive potential donors into believing that FFP was more efficient in using monetary gifts for charitable programs than it actually was.

LEGAL CONCLUSIONS

Legal Standards

1. The Attorney General has the primary responsibility for ensuring compliance with charitable fundraising laws and for protecting charitable assets, and "has broad powers under common law and California statutory law to carry out these charitable trust enforcement responsibilities. . . ." (§ 12598, subd. (a).) "Virtually every aspect of the activities of charities and their commercial fundraisers is subject to comprehensive regulation. The assets of nonprofit corporations . . . organized solely for charitable purposes, are impressed with a charitable trust which the Attorney General has a duty to protect. [Citation.]" (*People v. Orange County Charitable Services* (1999) 73 Cal.App.4th 1054, 1074.)

2. The first amended order alleges FFP violated California law by not maintaining its financial records in accordance with GAAP. For a charitable organization soliciting donations in California, "[t]he financial records of [the] soliciting organization shall be maintained on the basis of generally accepted accounting principles as defined by the American Institute of Certified Public Accountants, the Governmental Accounting Standards Board, or the Financial Accounting Standards Board." (Bus. & Prof. Code, § 17510.5, subd. (a).) The first amended order also alleges FFP violated California law by making deceptive representations in its charitable solicitations. "Regardless of injury, the following acts and practices are prohibited in the planning, conduct, or execution of any solicitation or charitable sales promotion: [¶] . . . [¶] (2) Using any unfair or deceptive acts or practices or engaging in any fraudulent conduct that creates a likelihood of confusion or misunderstanding." (§ 12599.6, subd. (f)(2).)

3. The Attorney General may revoke or suspend a charity's registration for violating the Supervision of Trustees and Fundraisers for Charitable Purposes Act, and may issue a cease and desist order for violating that act or the regulations adopted under it. (§§ 12591.1, subd. (b), 12598, subd. (e); Cal. Code Regs., tit. 11, § 314, subd. (a)(4).) The Attorney General may also impose an administrative penalty of up to \$1,000 for each act or omission constituting a violation. (§ 12591.1, subd. (c); Cal. Code Regs., tit. 11, §§ 315, 999.6, subd. (a)(3).)

4. The charity may appeal the Attorney General's administrative action, and the hearing on the appeal "shall be conducted in accordance with the procedures set out in Chapter 5 (commencing with section 11500) of Part 1 of Division 3 of Title 2 of the Government Code, except for provisions requiring the designation of administrative law judges." (Cal. Code Regs., tit. 11, § 999.6, subd. (e).) At the hearing, complainant bears the burden of proving the alleged violations by a preponderance of the evidence (Evid. Code, § 115), which means "evidence that has more convincing force than that opposed to it." [Citation.] (*People ex rel. Brown v. Tri-Union Seafoods, LLC* (2009) 171 Cal.App.4th 1549, 1567.)

5. FFP contends complainant must prove the alleged violations by clear and convincing evidence, but "[e]xcept as otherwise provided by law, the burden of proof requires proof by a preponderance of the evidence." (Evid. Code, § 115.) In administrative disciplinary proceedings concerning nonprofessional licenses, the burden of proof requires proof by a preponderance of evidence, not by clear and convincing evidence. (*Imports Performance v. Dept. of Consumer Affairs, Bureau of Automotive Repair* (2011) 201 Cal.App.4th 911, 916-917 (*Imports Performance*); *Ettinger v. Board of Medical Quality Assurance* (1982) 135 Cal.App.3d 853, 855-857; *Mann v. Dept. of Motor Vehicles* (1999) 76 Cal.App.4th 312, 319.) A charity registration is a nonprofessional license in that it requires no particular education, skill, training, or testing to obtain. (See *Imports Performance*, *supra*, 201 Cal.App.4th at pp. 916-917.) To the contrary, section 12585 requires every charitable corporation, unincorporated association, and trustee subject to the Supervision of Trustees and Fundraisers for Charitable Purposes Act to register with the Attorney General within 30 days of receiving charitable assets, without regard to such considerations. Therefore, FFP's contention that the clear and convincing evidence standard of proof applies is unpersuasive.

Discussion

GAAP COMPLIANCE

6. Complainant did not prove a GAAP violation by a preponderance of the evidence. The testimony of Ms. MacDonald and Mr. Richman about GAAP had more convincing force than Mr. Stevens's testimony, and supported the charities valuing the pharmaceutical donations according to United States market prices. Furthermore, the AICPA audit risk alert from 2018 is directly on point and supports the charities valuing the pharmaceuticals as they did. The charities' independently-audited financial statements also

supported the valuations by evidencing that multiple other accountants agreed with those valuations. (Factual Finding 22.)

7. In a case about GAAP and an entity's balance sheet, the United States Court of Appeals for the Ninth Circuit stated, "To determine whether the balance sheet is prepared in accordance with GAAP, we do not take off our judicial black robes and reach for the accountant's green eye shade." (*Bolt v. Merrimack Pharmaceuticals, Inc.* (9th Cir. 2007) 503 F.3d 913, 918.) In a case about GAAP and charity valuations of donated pharmaceuticals, an administrative hearing officer does not get to reach for the accountant's green eye shade either. Admittedly, using United States market prices to value donated pharmaceuticals that are restricted to distribution and use outside the United States is counterintuitive, and leads to annual revenue and expense figures for FFP that in some cases exceeded one billion dollars, making the charity seem artificially large. But determining FFP's compliance with GAAP depends on expert evidence, not on intuition. The charities' expert evidence of GAAP compliance was more persuasive than complainant's expert evidence of non-compliance.

SOLICITATIONS

8. Although complainant did not prove a GAAP violation, the evidence did prove that FFP used "deceptive acts or practices . . . that create[d] a likelihood of confusion or misunderstanding" in its solicitations. (§ 12599.6, subd. (f)(2).) FFP's solicitations were likely to deceive potential donors into believing that FFP was more efficient in using monetary gifts for charitable programs than it actually was. FFP's solicitations for monetary gifts stated that it used 95 percent of gifts for charitable programs, and were written in a manner implying that this percentage applied to the monetary gifts being solicited. But FFP really used less than 70 percent of monetary gifts for charitable programs, and used the rest for administration and fundraising. Potential donors were likely to be deceived by the percentage efficiency statements, which did not accurately represent FFP's efficiency in using monetary gifts for charitable programs. (See Factual Findings 23-31.)

9. No appellate court has interpreted section 12599.6, but the unfair competition law (UCL), Business and Professions Code section 17200 et seq., contains analogous provisions. The UCL statutes prohibit unfair, deceptive, or unlawful business practices, and section 12599.6 contains similar prohibitions with respect to charitable solicitations. In addition, section 12599.6, subdivision (f)(2), is analogous to the UCL in prohibiting unfair, deceptive, or fraudulent conduct "that creates a likelihood of confusion or misunderstanding." This is akin to the UCL's "likely to deceive" criteria, under which even a perfectly true statement may be actionable:

A business practice violates the law if it is "likely to deceive the public." [Citations.] It may be based on representations to the public which are untrue, and "also those which may be accurate on some level, but will nonetheless tend to mislead or

deceive A perfectly true statement couched in such a manner that is likely to mislead or deceive the consumer, such as by failure to disclose other relevant information, is actionable under” the UCL. [Citations.]

(*Patricia A. Murray Dental Corp. v. Dentsply International, Inc.* (2018) 19 Cal.App.5th 258, 271.) Therefore, cases interpreting the UCL provide useful guidance in interpreting section 12599.6.

10. Even if the percentage efficiency statements in FFP’s solicitations were technically accurate based on FFP’s reported financial information, those statements were deceptive because they implied that FFP used less than five percent of monetary gifts for administrative costs. A reasonable person would be likely to interpret the percentage efficiency statements in the solicitations that way. Under the UCL, a claim based on false or misleading advertising and unfair business practices must be evaluated from the vantage of a reasonable consumer, unless the advertisement targets a particular disadvantaged or vulnerable group. (*Lavie v. Procter & Gamble Co.* (2003) 105 Cal.App.4th 496, 506-509.) Similarly here, FFP’s charitable solicitations must be evaluated from the vantage of a reasonable person, who need not be “exceptionally acute and sophisticated” or “necessarily wary or suspicious” of the solicitations. (See *id.* at pp. 509-510.)

11. FFP’s argument that its percentage efficiency statements are true is not determinative, because even a true statement may be deceptive for the reasons described above. FFP also argues that because there are no reported complaints about its solicitations, no one has been deceived. But proof of actual deception or injury is not necessary, and donors who are unaware they are being deceived would not complain in any event.

12. FFP further argues there was insufficient proof of a violation because complainant conducted no investigation to confirm that donors would believe the percentages related only to cash donations. But the primary evidence in this charitable solicitation case is the solicitations themselves, just as “the primary evidence in a false advertising case is the advertisement itself.” (*Brockey v. Moore* (2003) 107 Cal.App.4th 86, 100 (*Brockey*); accord, *Hypertouch, Inc. v. ValueClick, Inc.* (2011) 192 Cal.App.4th 805, 839.) A consumer survey or similar evidence that misstatements would likely deceive a reasonable person is not required. (*Brockey, supra*, 107 Cal.App.4th at p. 100.)

13. Moreover, determining reasonableness is something the trier of fact – in this case, the administrative law judge – does in all types of cases. As indicated in *Brockey*, if “a person of ordinary intelligence could reasonably be deceived or confused, that is all that is required.” (*Brockey, supra*, 107 Cal.App.4th at p. 100, quoting *Hair v. McGuire* (1961) 188 Cal.App.2d 348, 353.) The trier of fact should not have to exclude himself or herself as a person of ordinary intelligence and a reasonable person. The solicitations speak for themselves, and the percentage efficiency statements in them implied facts about how FFP used its monetary donations that were untrue. Therefore, the administrative law judge is in a position to determine that the solicitations were likely to deceive a reasonable person.

FIRST AMENDMENT

14. FFP and the other two charities also argue that the orders against them violate their First Amendment rights to freedom of speech under the United States Constitution. But no appellate court has declared section 12599.6 unconstitutional, and the United States Supreme Court's opinions on charitable solicitation have taken care to leave a corridor open for actions to guard the public against false or misleading charitable solicitations. (*Illinois ex rel. Madigan v. Telemarketing Associates, Inc.* (2003) 538 U.S. 600, 617 (*Madigan*)). This is such an action.

15. The charities liken section 12599.6, subdivision (f)(2), to a statute invalidated in *Riley v. National Federation of the Blind of North Carolina, Inc.* (1988) 487 U.S. 781 (*Riley*), that compelled fundraisers to disclose to potential donors the percentage of the prior year's contributions that actually went to charity. (*Id.* at p. 795.) But section 12599.6, subdivision (f)(2), compels no speech; rather, it prohibits unfair, deceptive, or fraudulent acts or practices in the planning, conduct, or execution of any solicitations or charitable sales promotion. The Supreme Court has never held that the First Amendment protects such acts or practices in charitable solicitations. To the contrary, a state may vigorously enforce its antifraud laws to prohibit professional fundraisers from obtaining money on false pretenses or by making false statements. (*Riley, supra*, 487 U.S. at p. 800.)

16. *Riley, Village of Schaumburg v. Citizens for a Better Environment* (1980) 444 U.S. 620, and *Secretary of State of Md. v. Joseph H Munson Co., Inc.* (1984) 467 U.S. 947, each invalidated state or local laws that categorically restrained solicitation by charities or professional fundraisers if a high percentage of the funds raised would be used to cover administrative or fundraising costs. (See *Madigan, supra*, 538 U.S. at p. 610.) In contrast, section 12599.6 does not categorically restrain solicitation based on the percentage of funds used to cover administrative or fundraising costs, but rather seeks to protect California consumers from unfair, deceptive, or fraudulent acts or practices in charitable solicitations.

17. Citing *Madigan*, the charities argue that the First Amendment forbids the government from prohibiting false or misleading statements in charitable solicitations in the absence of proving common law fraud. *Madigan* authorized suit by Attorney General of Illinois against professional fundraisers for fraudulent charitable solicitations, holding that the government's "full burden of proof" of common law fraud "provided sufficient breathing room for protected speech." (*Madigan, supra*, 538 U.S. at pp. 615, 623-624.) But this holding does not mean the deceptive statements at issue are protected under the First Amendment, or that proof of common law fraud is required in every government action concerning charitable solicitations to provide the necessary "breathing room" for protected speech. (*Ibid.*)

18. Section 12599.6, subdivision (f)(2), requires that charitable solicitations be conducted without unfair, deceptive, or fraudulent acts or practices that create the likelihood of confusion or misunderstanding. California has a compelling interest in protecting its residents from such acts or practices in charitable solicitations, and section 12599.6 is

narrowly drawn to further that interest without interfering unnecessarily with First Amendment freedoms. Therefore, enforcing that statute in this case does not violate the First Amendment.

Disposition

CEASE AND DESIST ORDER

19. Complainant requests that the Attorney General affirm the order that FFP cease and desist from "including the '95% Statement' in its solicitations to California donors (or other percentages of combined cash and non-cash donations used for programs)." (Exhibit 1.4, First Amended Order to Cease and Desist against FFP at p. 8.) Complainant established that including the percentage statement violated section 12599.6, subdivision (f)(2); therefore, this cease and desist order is proper.

PENALTIES

20. In his closing brief, complainant requests \$100 in penalties per deceptive solicitation under section 12591.1, not to exceed the \$1,000,000 in penalties assessed for solicitation violations in the first amended order.

21. Section 12591.1 is silent regarding the criteria to consider in assessing the amount of the penalty, but the UCL provides useful guidance on the appropriate criteria: "In assessing the amount of the civil penalty, the court shall consider any one or more of the relevant circumstances presented by any of the parties to the case, including, but not limited to, the following: the nature and seriousness of the misconduct, the number of violations, the persistence of the misconduct, the length of time over which the misconduct occurred, the willfulness of the defendant's misconduct, and the defendant's assets, liabilities, and net worth." (Bus. & Prof. Code, § 17206, subd. (b).)

22. Complainant's request is reasonable and is far less than the \$1,000 per violation authorized by statute. (§12591.1, subd. (c).) Under the UCL, each act of false advertising constitutes a separate violation (*People v. Toomey* (1984) 157 Cal.App.3d 1, 21-23); by analogy, each deceptive solicitation in this case is a separate violation. Between just 2013 and 2015, FFP sent 948,958 solicitations containing these statements to persons in California. (Factual Finding 7.) Penalties of \$100 per solicitation would far exceed \$1,000,000, the amount assessed in the amended order.

23. FFP's direct mail solicitations to Californians were deceptive and created a likelihood of confusion or misunderstanding by California donors. The volume, persistence, and length of time during which FFP sent deceptive solicitations was substantial, as was the income FFP derived from the solicitations. The solicitations were worded so that potential donors would believe that less than five percent of monetary gifts would be used for fundraising and administrative costs, which was not the case. This conveyed a false sense of FFP's efficiency as a charity. Mr. Alexander's testimony that the percentages were accurate

when considering all of FFP's programs does not justify reducing the penalty below \$100 per solicitation. The solicitations were still deceptive. Furthermore, FFP has substantial annual income and the net worth and assets available to pay the requested penalty amount, according to its own financial records. (See Factual Finding 3.) Therefore, FFP will be ordered to pay the requested amount.

24. The first amended order also assessed \$88,000 in penalties against FFP for allegedly making materially false statements in its IRS Forms 990 and Forms RRF-1 and for failing to maintain its financial records in accordance with California law. Most of those penalties concerned FFP's alleged violation of GAAP in its financial records and reporting, which complainant did not prove. The remainder concerned FFP's alleged violation of an accounting concept called joint cost allocation, but complainant did not present evidence of such a violation at the hearing. Therefore, the additional \$88,000 in penalties will not be imposed.

CHARITY REGISTRATION

25. Complainant also requests revocation of FFP's charity registration, which would prohibit FFP from conducting any further charitable solicitation in California. While the Attorney General may revoke FFP's registration for the violations, the evidence does not support that result, for several reasons. First, complainant did not establish a GAAP violation, which was the focus of many of the allegations in the first amended order. Second, FFP has no prior disciplinary history with the Attorney General about its solicitations or otherwise. Third, no evidence suggested that FFP has continued to send out the types of deceptive solicitations at issue since receiving the first amended order. To the contrary, FFP's counsel represented that FFP stopped sending out solicitations containing the 95% Statement immediately. Fourth, while FFP deceptively misused the percentage efficiency statements, complainant did not prove that the misuse amounted to fraudulent conduct. Fifth, the cease and desist order and penalties themselves are significant and adequate deterrents against future solicitation violations. Therefore, the public will be adequately protected without revocation of FFP's charity registration. FFP should be given the chance to comply, with the understanding that further violations could lead to outright revocation of its registration.

ORDER

The First Amended Order to Cease and Desist is affirmed in the following respects:

1. FFP shall immediately cease and desist from including the "95% Statement" in its solicitations to California donors (or other percentages of combined cash and non-cash donations used for programs). This order applies to FFP, its officers, directors, employees, and all persons or entities acting on its behalf, including commercial fundraisers for charitable purposes soliciting on its behalf.

2. Within 10 days from the effective date of this order, FFP will provide a copy of this order to:

a. Every commercial fundraiser for charitable purposes and fundraising counsel for charitable purposes with which it currently contracts.

b. Every officer, director and employee of FFP;

3. Within 15 days from the effective date of this order, FFP shall provide written confirmation to the California Attorney General that it is in compliance with this order, including proof of service of the order as required by the preceding paragraph.

4. Within 30 days from the effective date of this order, FFP shall pay a penalty of \$1,000,000 to the California Attorney General.

DATED: May 24, 2019

DocuSigned by:
Thomas Heller
CFDEA01421714A4...

THOMAS HELLER
Administrative Law Judge
Office of Administrative Hearings

DECLARATION OF SERVICE BY E-MAIL and U.S. Mail

Case Name: **In the Matter of the First Amended Order to Cease and Desist and Assessment of Penalties Against:**

CATHOLIC MEDICAL MISSION BOARD, INC.

Case No.: **2018-13-5602319**

OAH No.: **2018050397**

Case Name: **In the Matter of the First Amended Order to Cease and Desist, Revocation of California Charity Registration and Assessment of Penalties Against:**

FOOD FOR THE POOR, INC.

Case No.: **2018-CT086331**

OAH No.: **2018050194**

Case Name: **In the Matter of the First Amended Order to Cease and Desist, Revocation of California Charity Registration and Assessment of Penalties Against:**

MAP INTERNATIONAL

Case No.: **2018-CT103136**

OAH No.: **2018050401**

I declare:

I am employed in the Office of the Attorney General, which is the office of a member of the California State Bar, at which member's direction this service is made. I am 18 years of age or older and not a party to this matter. I am familiar with the business practice at the Office of the Attorney General for collection and processing of correspondence for mailing with the United States Postal Service. In accordance with that practice, correspondence placed in the internal mail collection system at the Office of the Attorney General is deposited with the United States Postal Service with postage thereon fully prepaid that same day in the ordinary course of business.

On September 6, 2019, I served the attached **DECISIONS** by transmitting a true copy via electronic mail. In addition, I placed a true copy thereof enclosed in a sealed envelope, in the internal mail system of the Office of the Attorney General, addressed as follows:

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(By U.S. Mail only)

I declare under penalty of perjury under the laws of the State of California the foregoing is true and correct and that this declaration was executed on September 6, 2019, at San Francisco, California.

Kathleen M. McCormick

Declarant



Signature